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C O N F I D E N T I A L SECTION 01 OF 02 MADRID 001003

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b)

Contents:

Reactions to U.S. Financial Turmoil

¶1. (SBU) Spanish government officials and press followed the U.S. financial turmoil closely during the week. President Zapatero and Second Vice President and Economy and Finance Minister Solbes reassured Spaniards that Spain's financial sector was safe and its financial firms solvent. Zapatero claimed that the turmoil proved that the U.S. subprime mortgage crisis was the origin of Spain's difficulties. Solbes later acknowledged that Spain's housing and inflation problems predated the international credit crisis but said they would have been manageable without the credit crisis. Some of Zapatero's political allies described USG actions as proving the inadequacy of unregulated markets and the value of economic intervention.

¶2. (U) Solbes' ministry announced that Spanish financial firms had only limited direct exposure to Lehman Brothers. 62 insurance companies had 281 million euros in exposure, 0.2% of the sector's total exposure. 45 pension funds had exposure totaling 0.07% of assets, and investment funds had 300 million euros in Lehman bonds or shares, 0.13% of the sector's assets. Solbes and visiting European Commissioner for Economic and Monetary Affairs Joaquin Almunia called for more centralized EU financial supervision. (All Media)

2009 Budget to be Austere

¶3. (U) Secretary of State for Treasury and Budget Carlos Ocana announced September 18 that because of lower-than-expected growth, the 2009 budget will be more restrictive than the GOS had anticipated in June. Press reports suggest that the 2009 budget proposal the GOS is negotiating with parliamentary groups will include a deficit of 2% of GDP. (Europa Press, 9/18; El Pais 9/17)

Immigrant Return Incentive Approved

¶4. (U) The Council of Ministers approved Labor Minister Corbacho's proposal to allow unemployed immigrants to obtain all of their unemployment benefit if they agree to leave the country and not return for three years. Immigrants from the 19 non-EU countries that have Social Security agreements with Spain will be able to participate, receiving 40% of the benefit in Spain and the remaining 60% a month later in their country of origin. Of the 165,000 immigrants registered as unemployed in July, over half were from either Ecuador or Morocco. The incentive must be reviewed by the Council of State before it can take effect. (El Pais, 9/19; Council of Ministers, 9/19)

Energy Commission Fears Problems Unless GOS Increases Electricity Charges

¶5. (U) According to the National Energy Commission (CNE), if the GOS does not drastically increase electricity tariffs, then it runs the risk of accruing an additional debt of up to 5 billion euros in 2009 to add to the 9 billion it already has with electricity companies. Under Spain's partially liberalized electricity price system, tariffs for the captive markets are set by the government. Companies that serve this portion of the market often must sell electricity to consumers below cost, producing a deficit that runs into billions of euros which the GOS is obliged to reimburse. With a deficit of 9 billion (partially financed by private banks), the CNE fears that additional debt may incur serious financial difficulties. Energy Secretary-General Pedro Marin

told reporters that the next tariff increase would not take place until January. Comment: Given Spain,s economic woes and rising unemployment, the GOS will find it politically difficult to raise electricity prices by too much. The GOS, which has been under pressure from the European Commission to abolish regulated tariffs and from the CNE to raise tariffs, has said in the past that it needs several years to raise regulated prices enough to bring them fully in line with costs. Recent GOS tariff increases have been above the rate of inflation but below CNE requests. (Expansion, 9/18; ABC, 9/17, Embassy)

GOS on Track to Implement Radiation Detection Maritime Portals by Late 2009

¶6. (C) Spanish Customs officials told a DOE Megaports visiting team and Emboff September 15 that the GOS was on schedule to install radiation detection portals at the maritime ports of Valencia and Barcelona by late 2009. The GOS will shortly solicit bids from companies interested in undertaking this Megaports project at each port. The bidding and award process is expected to take 6 months, followed by the construction and installation, which is expected to take up to 9 months. The visiting DOE Megaports team was in Madrid September 15 to add final technical suggestions to the RFP document prepared by Spanish Customs. Comment: The only obstacle the GOS may face in implementing Megaports may be the upcoming year,s budget, which is expected to be strained given the current economic woes. (Embassy)

Vodafone Launches 670 Million Euro Suit Against Telefonica Subsidiary

¶7. (U) Vodafone has filed suit against Telefonica Moviles de Espana in Spanish court (1st instance court in Madrid) demanding reparation in the amount of 670 million euros. Vodafone asserts that Telefonica abused its dominant position in the mobile phone market between 1995-1999, blocking Vodafone,s Airtel from gaining access to its network and ultimately blocking Airtel from hundreds of millions of euros in profits. According to the Spanish press, Vodafone,s suit builds on the 2006 Supreme Tribunal,s decision that

determined that between 1996-1999, Telefonica engaged in conduct that blocked or hindered Airtel,s access to the network, conduct which did not comply with Spain,s law against anti-competitive practices (Ley de Defensa de Competencia).This is the largest judicial suit presented in Spain against a Spanish multinational company. (El Pais, 9/15)

Sabadell Sells Half of Insurance Business for 750M Euros

¶8. (U) Banco Sabadell, Spain's sixth largest banking institution, will sell half of its insurance business to Zurich Vida for 750 million euros plus the possibility of up to another 150 million euros over ten years, depending on the evolution of future business. Sabadell is following other Spanish banks that have sold or are studying selling part of their insurance business to raise funds. Comment: Spain's financial press gave this action very little coverage, which suggests that it was not a panic sale. Sabadell's stock price is down 40% from its peak of last year, but that is actually less of a drop than most Spanish banks have suffered. (Expansion, 9/19)

Aguirre